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## Energy Subsidies and the World Trade Organization

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### Introduction

In recent months the World Trade Organization (WTO) has seen increasing conflict over the rules for government support of the energy sector. Government subsidies for particular forms of energy have long influenced producers' investment choices and consumers' consumption patterns in ways that affect both international trade and the environment. Trade and environmental lawyers have thus closely watched the WTO's efforts to develop rules on government support for the energy sector. This *Insight* outlines recent activity in the WTO on subsidies for both traditional fossil fuels and the renewable energy sector. It also discusses the difficulties posed by the increased application of WTO subsidies rules to renewable energy subsidies at a time in which fossil fuel subsidies programs continue to elude significant WTO scrutiny. This discrepancy – caused in part by WTO rules on subsidies and in part by energy politics in a number of countries that have shifted support for renewable energy subsidies to local governments less skilled in drafting WTO-compliant programs – threatens to undermine the WTO's ability to develop an environmentally-friendly jurisprudence on energy trade issues.

### Fossil Fuel Subsidies

Government support for energy consumption has long been a target of environmental advocates. Traditionally, most environmentalists have focused their attention on eliminating subsidies for fossil fuels. This emphasis stems from estimates, such as that by Faith Birol, the chief economist at the International Energy Agency (IEA), that eliminating subsidies for coal, gas, and oil could produce half the greenhouse gas emissions reductions necessary to keep global warming under 2 degrees Celsius.<sup>[1]</sup> Environmentalists' efforts have borne some fruit at the political level. At the G20 Summit in Pittsburg in September 2009, leaders of G20 countries committed to "phase out and rationalize over the medium term inefficient fossil fuel subsidies," which the G20 blamed for "wasteful consumption, . . . impeding investment in clean energy sources and undermin[ing] efforts to deal with the threat of

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### DOCUMENTS OF NOTE

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climate change."<sup>[2]</sup> Despite this commitment, the IEA estimated that consumer subsidies increased to \$523 billion in 2011, an increase of over 30% from 2010.<sup>[3]</sup>

With political commitments seemingly inadequate to deal with fossil fuel subsidies, a turn to legal rules offers some promise. Concern about the need to reconcile WTO rules with the harmful environmental consequences of fossil fuel subsidies has been on the WTO agenda for some time. At a conference in 2010, WTO Deputy Director-General Harsha Vardhana Singh stated that "[r]eflections on the link between trade and climate change, and on the eventual role of the WTO rulebook on an issue such as fossil-fuel subsidies, must take place."<sup>[4]</sup> Despite this concern, however, little concrete action has taken place within the WTO to address fossil-fuel subsidy reform. To date, however, the WTO has not been at the forefront of fossil fuel subsidy reform. On April 29, 2013, outgoing WTO Director-General Pascal Lamy lamented that the "discussion on the reform of fossil-fuel subsidies has largely bypassed the WTO. This is a missed opportunity."<sup>[5]</sup>

The lack of action on fossil fuel subsidies can be explained both by political dynamics, in which producer states oppose new WTO disciplines on energy subsidies, as well as by the difficulty of applying existing WTO rules to fossil fuel subsidy programs. With respect to the latter, under the Agreement on Subsidies and Countervailing Measures (SCM Agreement) subsidies are prohibited if they are contingent upon either export performance or the use of domestic over imported goods.<sup>[6]</sup> Even if they are not prohibited, subsidies can still be actionable if they are "specific to an enterprise or industry or group of enterprises or industries within the jurisdiction of the granting authority" and cause adverse effects on the interests of other members.<sup>[7]</sup> Governments have periodically argued that fossil fuel subsidies – especially dual pricing schemes, under which governments set a lower price for domestic consumption of fossil fuels than the price charged for exported fuel – are either prohibited or at least actionable under these definitions.<sup>[8]</sup> Dual pricing, one of the forms of government support for fossil fuel consumption most commonly discussed at the WTO, is problematic from both an environmental and trade perspective. On the environmental side of the ledger, dual pricing encourages overconsumption of fossil fuels by lowering the price consumers pay. With respect to trade, it provides industries with cheaper energy inputs relative to the prices paid by competitors.

Arguments that dual pricing is inconsistent with WTO subsidies rules have not gained significant traction, however.<sup>[9]</sup> In order to be prohibited, dual-pricing schemes would have to link receipt of the preferential domestic price to either increased exports or the use of some domestic product over an imported one.<sup>[10]</sup> Regulations setting the domestic price of fossil fuels simply have to avoid imposing either of these conditions, a task that is not particularly onerous. Nor, with careful drafting, are dual pricing schemes likely to be deemed specific.<sup>[11]</sup> Specificity focuses on whether access to the subsidy is limited, either on a de jure or de facto basis, to certain enterprises or industries.<sup>[12]</sup> Dual-pricing schemes, though, usually apply to all industries and enterprises throughout the economy.<sup>[13]</sup> Thus, despite their negative environmental and trade consequences, dual-pricing schemes would be very difficult to challenge before the WTO. Those rules that have been developed for dual pricing have largely come by way of unilateral commitments made by states when joining the WTO.<sup>[14]</sup> For example, as part of its WTO accession negotiations with Europe, Russia agreed to increase its domestic natural gas prices, with a target of setting domestic prices in Russia equal to European "net of transport" prices by 2014.<sup>[15]</sup>

## **Renewable Energy Subsidies**

The inaction on fossil fuel subsidies at the WTO can be contrasted with the sharp increase in recent years in disputes over renewable energy subsidies. Global renewable energy subsidies totaled only \$88 billion in 2011 – roughly one sixth of fossil fuel subsidies.<sup>[16]</sup>

Despite this fact, four WTO disputes have been filed since 2010 challenging government programs supporting renewable energy, and a number of related disputes have yet to reach the WTO. Most of these disputes turn on the legality of requirements in government programs that renewable energy producers use domestic inputs in order to qualify for government support. These requirements, largely absent from fossil fuel subsidies programs such as dual pricing, potentially violate a number of WTO rules because they discriminate against imports in favor of domestic products.

The first such dispute was filed by Japan, later joined by the EU, in 2010 against Canada. Japan and the EU challenged a feed-in tariff program established by Ontario. The dispute centered on Ontario's decision to require the use of domestically-produced equipment for renewable energy generation facilities if such facilities wished to receive guaranteed prices under Ontario's Feed-In Tariff Programme. Japan alleged that the domestic content requirements violated the rule in article III:4 of the General Agreement on Tariffs and Trade 1994 (GATT) that internal regulations not discriminate in favor of domestically-produced products (the national treatment obligation) and the Agreement on Trade-Related Investment Measures (TRIMs) article 2.1 prohibition on trade-related investment measures violating GATT article III.<sup>[17]</sup> Japan and the EU also challenged the program as a prohibited subsidy under articles 3.1(b) and 3.2 of the SCM Agreement on the grounds that the benefit was a subsidy the receipt of which was conditioned on the use of domestic products over imported products.<sup>[18]</sup>

On December 19, 2012, the panel circulated a report ruling in complainants' favor as to the national treatment claims, finding that the domestic content requirements did indeed accord less favorable treatment to imported products in violation of GATT article III:4 and TRIMs article 2.1.<sup>[19]</sup> However, in a divided opinion the panel found that Japan and the EU had failed to carry their burden of showing that the guaranteed prices offered by the Feed-In Tariff Programme were a "benefit," as required by the SCM Agreement for a finding that the government measure at issue is a subsidy.<sup>[20]</sup> The Appellate Body report, adopted on May 24, upheld the panel's ruling in favor of the EU and Japan on the grounds that Ontario's program discriminated against imports, but did not reach a definitive conclusion with regard to the subsidy issue.<sup>[21]</sup>

Following hard on the heels of the *Canada-Renewable Energy* dispute, on February 6, 2013, the United States requested consultations (the first step in a WTO dispute) with India regarding the Jawaharlal Nehru National Solar Mission (NSM) program. The United States alleges that the NSM program requires solar power generators in India to use solar cells and modules of domestic origin in order to qualify for benefits in the form of long-term tariff rates for electricity, in breach of the same provisions at issue in *Canada - Renewable Energy*.<sup>[22]</sup> Shortly thereafter, on April 17, India filed documents with the WTO asking the United States to explain how a number of state and local incentive programs for renewable energy are consistent with the same set of WTO obligations – GATT article III:4, TRIMs article 2.1, and the SCM Agreement.<sup>[23]</sup> Such requests for information can be a precursor to the initiation of a formal dispute. In its filing, India identified five state and local renewable energy programs that raise concerns: Michigan's 2008 Clean, Renewable, and Efficient Energy Act; the Los Angeles Department of Water and Power's Solar Photovoltaic Incentive Program; the State of California's Self Generation Incentive Program; and the Commercial Solar Photovoltaic Performance-Based Incentive Program as well as the Residential Solar PV Rebate Program offered by Austin Energy, a publicly-owned power company and a department of the City of Austin, Texas.<sup>[24]</sup> As with the complaints against Canada and India, India's concern about these American programs centers on domestic content requirements.

A second string of disputes involves China. In December 2010 the United States requested

consultations with China regarding domestic content requirements for Chinese government programs offering grants, funds or awards to enterprises manufacturing wind power equipment (the EU and Japan later requested to join the consultations).[25] While China removed the precise subsidies at issue in that complaint, the United States has subsequently taken domestic action against Chinese imports of both wind towers and solar panels. With respect to wind, in December 2012 and January 2013, respectively, the U.S. Commerce Department and International Trade Commission (ITC) issued final rulings necessary to permit the Commerce Department to impose anti-dumping and countervailing duties on Chinese (and Vietnamese) imports of wind towers.[26] With respect to solar panels, the Commerce Department and ITC made final rulings authorizing the imposition of anti-dumping and countervailing duties against Chinese imports of silicon solar panels in October and November 2012.[27]

On the other side of the Atlantic, the European Commission initiated an anti-dumping investigation into Chinese solar panels in September 2012.[28] At the same time, the EC received a complaint from an industry group, EU ProSun, alleging that Chinese solar panel producers benefit from unfair government subsidies. On November 8, 2012, the EC took action on the complaint by launching an anti-subsidy (i.e., countervailing duty) investigation into Chinese subsidies.[29] On November 5, 2012, China responded to the European investigations by requesting consultations with the EU, Italy, and Greece.[30] China alleges that certain renewable energy measures throughout the EU, and specifically in Italy and Greece, contain domestic content requirements that violate GATT article I (most-favored nation), as well as GATT III, TRIMs article 2, and the SCM Agreement's ban on domestic content requirements as a condition for receipt of a subsidy.[31] On April 27, 2013, the EC announced a second anti-subsidy investigation into Chinese solar glass, a product distinct from the solar panels that were the target of the 2012 investigation. Solar glass is used primarily but not exclusively in the making of solar panels.[32] The tensions between Europe and China appear to be waning somewhat, though. On July 27, the European Union announced it had reached a tentative settlement with China over the solar panel dispute that would impose a minimum price on Chinese solar panels.[33]

### **Local versus National Subsidies Programs**

This string of complaints and counter-complaints – along with the relative absence of WTO disputes regarding fossil fuel subsidies – raises the possibility that the WTO disputes process will be used to develop a jurisprudence that limits government support for environmentally-friendly renewable energy programs without creating similar pressure on governments to limit support for environmentally-harmful fossil fuel subsidies. Further complicating the picture is the fact that many of the governmental measures at issue have been adopted by subnational governments (for example, Ontario in *Canada – Renewable Energy* and Michigan and other U.S. states where India is concerned). This development is significant because it means that the politics of renewable energy subsidies programs may make them more vulnerable to WTO challenges than fossil fuel subsidies.

As climate change negotiations have faltered, political support for climate-friendly measures, especially in countries not party to the Kyoto Protocol such as the United States and Canada, have shifted to local and regional governments. National governments may not be in a position to oversee the design of subsidies programs by local and regional governments. And while WTO members are of course responsible for the actions of local and regional governments, such subnational governments are likely to be less aware of WTO rules restricting domestic content requirements. Climate-friendly subsidies thus risk being targeted at the WTO precisely because such measures are more frequently designed by local policymakers eager to provide benefits to constituents and unschooled in ensuring their program's WTO-compatibility. Fossil-fuel subsidies, by contrast, are often national

policies. They are therefore more likely to take into account WTO rules in their design and to have the diplomatic backing of their governments in deterring WTO challenges. The application of WTO subsidies rules to energy thus risks discouraging subsidies for renewable energy development while doing little to reduce the remaining support for fossil fuel subsidies.

## Conclusion

The existence of domestic content requirements in renewable energy programs is likely a political condition for passage by governments that wish to show that they are not subsidizing foreign investors. But this political necessity has rendered government support for environmentally-helpful renewable energy programs vulnerable to challenge before the WTO in a way that environmentally-harmful fossil-fuel subsidies are not, creating tension once again between trade and climate objectives.

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## Endnotes:

[1] Duncan Clark, *Phasing out fossil fuel subsidies 'could provide half of global carbon target'*, The Guardian, Jan. 19, 2012, available at <http://www.theguardian.com/environment/2012/jan/19/fossil-fuel-subsidies-carbon-target>.

[2] Group of 20, *Leaders' Statement*, The Pittsburgh Summit ¶ 24 (Sept. 24-25, 2009), available at [http://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh\\_summit\\_leaders\\_statement\\_250909.pdf](http://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh_summit_leaders_statement_250909.pdf).

[3] Int'l Energy Agency, *Energy Subsidies*, <http://www.worldenergyoutlook.org/resources/energysubsidies/>.

[4] Harsha Vardana Singh, Deputy Director-General, WTO, *Address at the Opening of a Joint Conference by the Global Subsidies Initiative and the International Institute for Sustainable Development and UNEP* (Oct. 14, 2010), [http://www.wto.org/english/news\\_e/news10\\_e/ddg\\_14oct10\\_e.htm](http://www.wto.org/english/news_e/news10_e/ddg_14oct10_e.htm).

[5] Pascal Lamy, Director-General, WTO, *Remarks to the Workshop on the Role of Intergovernmental Agreements in Energy Policy* (Apr. 29, 2013), available at [http://www.wto.org/audio/wks24042013\\_dgpl.mp3](http://www.wto.org/audio/wks24042013_dgpl.mp3) (audio recording).

[6] Agreement on Subsidies and Countervailing Measures art. 3, Apr. 15, 1994, 1867 U.N.T.S. 14 [hereinafter SCM Agreement].

[7] *Id.* arts. 1.2, 2, 5.

[8] Yulia Selivanova, *The WTO and Energy: WTO Rules and Agreements of Relevance to the Energy Sector*, ICTSD Programme on Trade and Env't, 11-12 (2007), available at <http://dSPACE.cigilibrary.org/jspui/bitstream/123456789/28428/1/The%20WTO%20and%20energy.pdf?1> [hereinafter *WTO and Energy*].

[9] See, e.g., Yulia Selivanova, *International Energy Governance: The Role of the Energy Charter*, 106 ASIL Proc. 394, 395 (2012) (noting that "energy dual pricing has been perceived (unconvincingly) by some WTO members to be inconsistent with WTO rules").

[10] *WTO and Energy*, *supra* note 8, at 29.

[11] Other kinds of subsidies, such as corporate tax breaks available only to companies in energy industries, are more likely to be deemed specific. Careful drafting of the subsidies rules, however, can make a claim of specificity more difficult to maintain.

[12] SCM Agreement, *supra* note 6, art. 2.

[13] *WTO and Energy*, *supra* note 8, at 29.

[14] Gabrielle Marceau, *The WTO in the Emerging Energy Governance Debate*, 106 ASIL Proc.



[15] Peter Milthorpe & David Christy, *Energy Issues in Selected WTO Accessions, in Regulation of Energy in International Trade Law* 259, 293 (Yulia Selivanova ed., 2011).

[16] Int'l Energy Agency, *World Energy Outlook 2012* 211 (Nov. 12, 2012), available at [http://www.worldenergyoutlook.org/media/weowebbsite/2012/WEO2012\\_Renewables.pdf](http://www.worldenergyoutlook.org/media/weowebbsite/2012/WEO2012_Renewables.pdf).

[17] Article 2.1 provides that "no Member shall apply any TRIM that is inconsistent with the provisions of Article III or Article XI of GATT 1994."

[18] Appellate Body Report, *Canada-Certain Measures Affecting the Renewable Energy Generation Sector, Canada-Measures Relating to the Feed-In Tariff Program*, 17-19, WT/DS412/AB/R, WT/DS426/AB/R (May 6, 2013), available at [http://www.wto.org/english/tratop\\_e/dispu\\_e/412\\_426abr\\_e.pdf](http://www.wto.org/english/tratop_e/dispu_e/412_426abr_e.pdf) [hereinafter Appellate Body Report].

[19] Panel Report, *Canada-Certain Measures Affecting the Renewable Energy Generation Sector, Canada-Measures Relating to the Feed-In Tariff Program*, ¶ 7.167, WT/DS412/R, WT/DS426/R (Dec. 19, 2012).

[20] *Id.* ¶ 7.327.

[21] Appellate Body Report, *supra* note 18, ¶¶ 6.1, 5.246.

[22] See Request for Consultations by the United States, *India – Certain Measures Relating to Solar Cells and Solar Modules*, WT/DS456/1, G/L/1023 G/TRIMS/D/35, G/SCM/D96/1 (Feb. 11, 2013), available at <http://www.wto.org/tw/SmartKMS/fileviewer?id=131133>.

[23] Tom Miles, *India Questions U.S. Green Energy Incentives at WTO*, Reuters (Apr. 17, 2013), available at <http://uk.reuters.com/article/2013/04/17/us-india-usa-trade-idUKBRE93G11U20130417>.

[24] *Id.*

[25] Request for Consultations by the United States, *China – Measures Concerning Wind Power Equipment*, WT/DS419/1, G/L/950, G/SCM/D86/1 (Jan. 6, 2011).

[26] See *Utility Scale Wind Towers from China and Vietnam* (Investigation Nos. 701-TA-486 and 731-TA-1195-1196 (Final), USITC Publication 4372, February 2013), available at [http://www.usitc.gov/publications/701\\_731/pub4372.pdf](http://www.usitc.gov/publications/701_731/pub4372.pdf).

[27] See *Crystalline Silicon Photovoltaic Cells and Modules from China* (Inv. Nos. 701-TA-481, 731-TA-1190, USITC Pub. 4360 (Nov. 2012) (final), available at [http://www.usitc.gov/publications/701\\_731/pub4360.pdf](http://www.usitc.gov/publications/701_731/pub4360.pdf); see also Diane Cardwell, *Solar Tariffs Upheld, but May Not Help in U.S.*, N.Y. Times (Nov. 7, 2012).

[28] Press Release, European Commission, EU Initiates Anti-Dumping Investigation on Solar Panel Imports from China, (Sept. 6, 2012), [http://europa.eu/rapid/press-release\\_MEMO-12-647\\_en.htm](http://europa.eu/rapid/press-release_MEMO-12-647_en.htm).

[29] Press Release, European Commission, EU Initiates Anti-Subsidy Investigation on Solar Panel Imports from China (Nov. 8, 2012), [http://europa.eu/rapid/press-release\\_MEMO-12-844\\_en.htm](http://europa.eu/rapid/press-release_MEMO-12-844_en.htm).

[30] Argentina has also requested consultations with EU regarding support and protection for the biodiesel industry in alleged violation of a variety of GATT provisions, including articles 3.1 and 3.2 of the SCM Agreement. See Request for Consultations by Argentina, *European Union and Certain Member States – Certain Measures On the Importation and Marketing of Biodiesel and Measures Supporting the Biodiesel Industry*, G/L/1027, G/SCM/D97/1, G/TBT/D/44, G/TRIMS/D/36, WT/DS459/1 (May 15, 2013), available at <http://www.wto.org/tw/SmartKMS/fileviewer?id=133373>.

[31] Request for Consultations by China, *European Union and Certain Member States – Certain Measures Affecting the Renewable Energy Generation Sector*, WT/DS452/1; G/L/1008; G/SCM/D95/1; G/TRIMS/D/34 (Nov. 7, 2012), available at [http://trade.ec.europa.eu/doclib/docs/2012/november/tradoc\\_150099.pdf](http://trade.ec.europa.eu/doclib/docs/2012/november/tradoc_150099.pdf).

[32] Press Release, European Commission, EU Launches Anti-Subsidy Investigation on Solar Glass from China, (Apr. 27, 2013), [http://europa.eu/rapid/press-release\\_MEMO-13-386\\_en.htm](http://europa.eu/rapid/press-release_MEMO-13-386_en.htm).

[33] James Kanter & Keith Bradsher, *Europe and China Agree to Settle Solar Panel Fight*, N.Y. Times, July 27, 2013, available at <http://www.nytimes.com/2013/07/28/business/global/european-union-and-china-settle-solar-panel-fight.html>.